LC No. 5A06
HB/SB ____[1]

REPORT AND RECOMMENDATION OF THE STATE ADMINISTRATION AND VETERANS' AFFAIRS INTERIM COMMITTEE (SAVA) TO THE 2013 LEGISLATURE AS OF NOVEMBER 2012[2]

Proposal No. 10
Proposing Entity: Governor Schweitzer
Short Title: Improve actuarial funding for TRS

Retirement system affected
Teachers' Retirement System (TRS)

Proposal summary
According to the TRS FY 2012 actuarial valuation, the TRS unfunded liabilities do not amortize. In order to amortize the unfunded liabilities in 30 years (which has been the accepted standard for an actuarially sound pension system), an additional 4.89% of covered payroll (or about $36 million) must be contributed to the plan annually.

This proposal:

- creates a new membership tier, with tier two members those hired on or after 7/1/13;
- provides additional funding from three sources;
  - additional state funding from an annual flat dollar cash infusion from school trust land revenue ($25 million each year);
  - additional school district funding from a one-time only contribution from school district retirement fund reserves ($14.7 million one time); and

[1] This report summarizes SAVA's recommendation to the Legislature as of November 2012. The report is not a summary of a bill, but of a retirement proposal as presented to SAVA during the interim. The specifics of the proposal summarized may have changed during the subsequent drafting and legislative processes.

[2] Report issued pursuant to 5-5-228, MCA.

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- a 1% employee contribution increase with three parts to it:
  -- an adjustable 1% contribution increase for tier one members (hired before 7/1/13) that the board may decrease when the plan is 90% funded and unfunded liabilities may be amortized in less than 15 years; and

  -- a 1% contribution increase for tier two employees (hired after 7/1/13);

  -- a potential future contribution increase of up to 0.5% that the board may impose on tier two employees beginning Jan. 1, 2023, but only if the employer contribution is also increased by a matching amount.

- changes benefits for tier two employees (hired after 7/1/13):
  - increases the benefit multiplier to 2% for 30 or more years of service;
  - increases the period for calculating highest avg. compensation to 5 years of service;
  - increases normal retirement eligibility from 25 years to 30 years of service and age 60;
  - increases early retirement eligibility to age 55;
  - tightens disability benefit provisions; and
  - tightens death benefit provisions.

Fiscal implications

According to the system's actuarial analysis, the amortization schedule for the plan's unfunded liabilities will be reduced from "does not amortize" to amortizing the unfunded liabilities in 45 years.[3]

Effect on other Montana retirement systems

The TRS retirement eligibility change differs from what is provided in PERS. In the Public Employees' Retirement System (PERS), eligibility for normal retirement is:

- for tier one employees (hired before 7/1/11):
  - age 60 with at least 5 years of service;
  - age 65 regardless of service; or
  - 30 years of service regardless of age.

- for tier two employees (hired on or after 7/1/11)
  - age 65 with at least 5 years of service; or
  - age 70 regardless of service.

[3] The Legislative Fiscal Division has written a more detailed fiscal analysis for the Legislative Finance Committee, which maintains a website with links to it's reports at www.leg.mt.gov, selection "Fiscal" from the top menu and navigate to the Legislative Finance Committee meeting for November 13, 2012.

The TRS benefit multiplier change adds a tier in TRS that is similar to what is provided for PERS employees with 30 years or more of services. In PERS, there are three tiers to the benefit multiplier, as follows:

- for less than 10 years of service, the multiplier is 1.5%;
- for more than 10 but less than 30 years of service, the benefit is the greater of 1.786% per year of service or the actuarial equivalent of double the member's accumulated contributions; or
- for 30 or more years of service, the benefit is the greater of 2% per year of service or the actuarial equivalent of double the member's accumulated contributions.

Regarding early retirement, this proposal's change in eligibility to 5 years and age 55 will make TRS the same as PERS.

The proposal would also make the calculation of final average compensation for new hires using a 5-year average the same as the period used in PERS.

Soundness as matter of retirement policy

The proposal relates to the following policy principles and guidelines adopted by SAVA on January 27, 2012:

- Principle I - pensions should provide a financial base in retirement;
- Principle II - pension funding should be a contemporary obligation; and
- Guideline V - the legislature should resist changes to retirement benefit formulas or retirement eligibility criteria that would encourage early retirement.

The proposal also relates to the requirement in Montana's Constitution that the public retirement systems be funded on an "actuarially sound basis"[4] and the statutory requirement that unfunded liabilities be amortized in no more than 30 years[5], which has been one of the actuarial standards for determining whether a plan is actuarially sound.

The longer the legislature postpones funding the system's benefit obligations, the less contemporary the funding obligations become.

The proposal would provide retirees who remain working for 30 years or more with a 60% income replacement ratio and would thus would encourage members to work longer rather retire early.

Comparison with other states

Many states are in the process of revising their public pension plans due to the national financial crisis that created record investment losses for pension plans throughout the country.

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[4] Article VIII, Section 15, Montana Constitution.

[5] Section 19-2-409, MCA.

According to a National Conference for State Legislatures (NCSL), of the states that revised their pensions between 2009 and 2011 with respect to retirement eligibility requirements, most states:

- required new members to reach a certain age in addition to meeting years of service criteria;
- increased the age for retirement eligibility to age 65 or age 67; and
- increased or retained a 30 years of service requirement.[6]

Of 43 states who enacted major pension plan changes between 2009 and 2011, 33 states enacted higher age and service requirements for normal retirement eligibility, 17 states reduced their benefit multipliers, and many states increased the number or months or years used to calculate final compensation, and 32 state reduced early retirement benefits.[7] Thus, the changes proposed fall into line with what many other states are doing, except with respect to increasing the benefit multiplier to 2%.

Legal implications[8]

The adjustable 1% increase in contributions required from current employees may raise contract impairment issues.

Testimony received

The proposal was presented by Governor Schweitzer's budget director, Mr. Dan Villa, and was supported by the Teachers' Retirement Board and MEA-MFT. The Teachers' Retirement Board would also support this bill as a "By Request of" agency if the bill is moved forward.

There were no opponents to the proposal.[9]

Committee discussion

The committee requested that the preamble be strengthened and voted 7 to 1 (Sen. Lewis voting no) to continue to consider the bill as a committee bill and to ask the Legislative Finance Committee for its comments and recommendations.[10]

Recommendation

Will be considered by SAVA November 16, 2012.

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[6] Ronald K. Snell, "Changes in Age and Service Requirements for Normal Retirement in State Retirement Plans, 2009-2011", National Conference for State Legislatures, March 2012.

[7] Ibid.

[8] David Niss, Legal Memorandums dated May 21, 2012, January 5, 2012, August 14, 2009, August 28, 2009 (Addendum), and February 27, 1998, Montana Legislative Services Division, (406) 444-3064, or visit www.leg.mt.us and contact staff for the State Administration and Veterans' Affairs Interim Committee.

[9] State Administration and Veterans' Affairs Interim Committee (SAVA), September 11, 2012. Audio/video and summary minutes available at http://www.leg.mt.gov/, navigate to interim committees, SAVA, 2011-12 .

[10] Ibid.